FINANCIAL DIGITALIZATION FOR CONSUMERS, COMPANIES AND FINANCIAL INSTITUTIONS – KEY TRANSFORMATIONS

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Abstract:

In this paper we explore the most important changes that financial digitalization imposes on the activity of individuals, companies and financial institutions. We evaluate these changes through the lens of financial literacy and education, in order to draw conclusions regarding the importance of financial education during the digitalization of the economy. Key transformation factors are identified and presented in a structured manner, in order to facilitate future research. This paper builds on existing research in the field and also contributes to the relevant literature with a fresh perspective on current financial transformations.

Keywords: *digitalization, financial literacy, financial education*

JEL classification: *D14, G50, O33*

Introduction

The link between the financial system and technology is not recent. However, the unprecedented development of information technology leads to a very powerful merger. The digitalized trajectory of the financial system promises to reveal numerous opportunities and also important risks and threats.

Technology has changed the financial system and the way people and businesses interact with it. There is a lot of talk about how technological changes have brought the financial system closer to many people who did not have access to it before. However, this is only one facet of the change. It is easy to see how it has fundamentally changed and how other users interact with actors in the financial system. Technology has had a dual impact on the financial system: on the one hand it has transformed segments of the financial system through the digitalization process and on the other hand it has created new segments (Ciumara, 2020). This is a trend that promises to last long into the future, being therefore an important study area.

As already mentioned, technology brings the financial system closer to people. In recent years, smart phones have played a very important role in this regard. The increase in financial inclusion has obvious positive effects, but it also raises some problems for which adequate solutions must be found: digitization implies that more and more people with little financial education become beneficiaries of financial services, but they do not have the necessary knowledge to protect themselves from risks associated cybernetics.

The direction towards which the financial system is heading in the context of technological changes is relatively clear. We don't know exactly how the financial landscape will change in the next 5 or 10 years, but we know the main coordinates. The pandemic that appeared in

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2020 contributed to accentuating the digitization process and enhancing the conditions favoring the development of FinTech, making people go through a process of "forced digitization". Probably, many investors have redirected their funds from "brick and mortar" investments to investments based on digitized solutions. We will see in the coming years what the exact consequences of this crisis are, but at this point we can anticipate that they will be substantial. As mentioned, the "forced" digitization of a high proportion of the population fuels the demand for FinTech solutions. As the pandemic eases, the habits acquired during the period of social distancing take root more strongly, consolidating the adoption of a financial behavior with a more important digitized component.

Description of the Problem

The core premise for this paper is that financial digitalization is not the actual goal of the process but a means to an end, the way to make industry players reach their goals. This process certainly has a transformative impact on the financial behavior of both clients, be they individuals or companies and financial services providers. An in-depth look at how the financial landscape is impacted by digitalization is taken by Feyen et al (2021).

One study that explores the use of financial digital channels by consumers is that of Valverde and Fernández (2020).

Methodology and Data

This paper is based on analytical research of the topic, with an investigation of the evolution of services, products and practices related to the financial institutions, from the perspective of the institutions themselves and their clients, individuals or companies. We use data from previous studies on financial digitalization (Arner et al, 2015), financial behavior (Korobov, 2020) and financial literacy (Lusardi, 2019), to structure the key transformations based on temporal segmentation.

Results

We structure our results based on the type of stakeholder – consumers, companies and financial institutions – and the time sequence – past, present or future. This approach allows a better perspective on the manner in which financial digitalization makes an impact on society in general.

Financial digitalization for consumers

Past

- Adoption of non-bank payment options (PayPal);
- Increased credit options;
- More direct access to securities markets;
- Cheaper access to payment options;
- Possibility to make faster payments, including in international purchases;
- Face new threats to financial security (ex. phishing);

Present

- Augments consumer independence;
- Modifies the model of consumer behavior (Korobov, 2020), in the sense that the financing institutions is chosen after the product or service that needs to be financed is

found, as opposed to the manner things worked traditionally;
- Access to more diverse investment options;
- Financial services better suited to individual needs;

Future
- Increased access to finance;
- Faster access to financial services;
- Provide better chance for financial inclusion;
- Increase the gap between the financially literate and the financially illiterate;
- Need to take control of their data (not just financial data) in order to optimize their financial persona;
- Polarization of customers based on technology adoption speed;

Financial digitalization for companies

Past
- New options to receive payments from clients;
- Faster international payments;
- Cheaper international payments;

Present
- Faster access to financial services;
- Cheaper access to financial services;
- Access to more diverse financial services;
- Improved processes made possible by the new financial options (such as self-check-out at stores);
- Need to adopt procedures for safe digital financial operations;

Future
- Increased access to finance.;
- Financial services better suited to company needs;
- Data driven financial decision making;
- Real-time financial reporting impacting financing cycles;

Financial digitalization for financial institutions

Past
- Introduction of online banking services;
- Emergence of electronic transactions between financial institutions;
- Initial changes in the regulatory environment addressing digital services;

Present
- Transition of the online operations from the brick-and-mortar business model to a digital business model;
- Increase operational efficiency;
- Reduced cost barriers for market entry;
- Need to focus on cyber security aspects;
- Emergence of the Fintech industry;

Future
- Development of new services;
- Shift from spending on human capital to investing in technology;
- Changing regulatory framework;
- Restructuring of the industry, with Fintech players gaining market share.

Conclusions

We observe that the impact of financial digitalization is noticeable on various aspects of the interaction between consumers, companies and financial institutions with the financial system. As technological progress accelerates this impact changes.

Digitalization has a profound influence on finance. The opportunities presented by the acceleration of innovation in the field are multiple, both in terms of developing better services and products, as well as streamlining the way in which they are offered. The adoption of technological innovations in the field of finance is not homogeneous globally, largely depending on the degree of development of the states and social and cultural aspects.

Digital disruptions transform business models in all industries. There is no doubt that technological developments will continue to significantly influence the financial system and that these influences will accelerate in the years and even decades ahead. It is not clear whether these developments will have a homogenizing effect on financial inclusion or, on the contrary, the gap between regions or between those with different degrees of financial sophistication will increase. There are arguments in favor of both directions. Access to finance also depends on the level of financial education. The general level of financial education conditions both the demand and supply of financial services and products available throughout the economy. More financially sophisticated entrepreneurs diversify the range of financing instruments they consider. But if the number of these entrepreneurs is too small, the potential financiers are not in a position to have sufficiently diversified their offer of services and products.

As the complexity of the financial system increases, financial literacy becomes more important than ever. Financial institutions make efforts to improve the level of financial literacy because this way they support the development of their own business.

Technological changes lead to a transfer of financial activity from the physical to the virtual sphere. Although the services may be offered in a virtual environment, the companies have a physical location and respond to legislative requirements in certain countries. In the situation of companies that carry out activities in multiple countries, offering financial services and products of a homogeneous nature but with the application of different regulatory regimes raises particular difficulties.

The potential of technology to increase the level of financial inclusion is major. Although technological innovations are frequent and significant, even the use of old technologies, already considered obsolete in more developed regions, allows increasing the level of financial inclusion.

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